Agriculture Financial Services Corporation's (AFSC)

# QUARTERLY REPORT

## 2016-17

**(First Quarter Update - as of July 31, 2016)**

AFSC is in the business of helping Albertans achieve prosperity and build successful businesses.

**First Quarter Update - 2016-17**
**Agriculture Financial Services Corporation**

## Nature of Operations

Agriculture Financial Services Corporation (AFSC) is a crown corporation that is in the business of helping rural Albertans achieve prosperity and build successful enterprises. By providing strategic risk management and income stabilization programs for farm clients, and forward-thinking lending programs for both urban and rural entrepreneurs, AFSC provides Alberta businesses with the valuable tools they need to thrive.

## Overview

### Economic Climate

Over the first quarter, international agricultural markets were impacted by South American weather events, global supply and the international political environment. Dry conditions in Brazil and wet conditions in Argentina gave strength to commodity prices, and created good forward-marketing opportunities for Alberta producers. In addition to the favourable marketing opportunities, optimal growing conditions at the start of the crop season have producers optimistic for an excellent harvest. While agricultural commodities rallied for most of the quarter, a continual global oversupply placed downward pressure on agricultural markets near the end of June.

The wildfire that destroyed portions of Fort McMurray in May also impacted Alberta's energy sector due to halted oil sands production in the region. This wildfire is declared Canada's most costly disaster and resulted in the energy industry losing approximately $1.6 billion in revenue. The oil sands shutdown was just one of many international crude supply disruptions that pushed the price of West Texas Intermediate (WTI) to new highs over the quarter, breaking the $50 USD/bbl barrier in early June. Even though the rally in energy prices has spurred some optimism, the energy sector remains challenged. Investment in both conventional and non-conventional drilling continues to trend downward, leading to more job losses and weakness in other parts of the Alberta economy. In addition, global uncertainty caused by international events like Brexit and the United States political environment has created uncertainty in financial markets.

### Annual Crop Conditions

A warm, dry winter provided insufficient snow to cover and seal the soil in order to preserve the early moisture that crops require. The snow that was on the ground was quick to disappear in March, which provided producer's with an early opportunity to start seeding in many areas. By May 3, 21 per cent of the province was seeded, which was well ahead of both the five-year average (nine per cent) and the long-term average (15 per cent).

By the end of May, seeding was 97 per cent complete. This figure is two per cent behind last year's pace, and on par with both the five-year average of 96 per cent and the long-term provincial average of 94 per cent. However, crop growth was slowed by cool conditions. At the end of May 78 per cent of crops were above ground with 86 per cent of the spring wheat, 95 per cent of the durum, 71 per cent of the barley and 70 per cent of the canola emerged.

Warm weather during the first two weeks of June brought crop growing conditions up to 80 per cent good to excellent, an eight per cent increase over the five-year average (2011-2015). Specifically, 83 per cent of spring wheat, 81 per cent of barley, 88 per cent of oats, 75 per cent of canola, 82 per cent of dry peas, 91 per cent of potatoes and 95 per cent of sugar beets were reported to be in good to excellent condition.

Crops provincially were rated 79 per cent in good or excellent condition, compared to last year at 30 per cent, the five year average of 73 per cent and the long term average of 70 per cent.

## Perennial Crop Conditions

In April, hay and pastures were slow to start due to cool weather and dry soil. However, precipitation during the last two weeks of April resulted in significantly improved hay and pastures by the end of May. By mid-June, pasture and hay fields were in good condition, and by the end of the month haying was underway in practically all areas of the province. Twenty per cent of the first cut dryland crop and 35 per cent of the first cut irrigated alfalfa crop were baled by the end of the quarter. Hay yields are below average due to a slow start to growth this spring caused by cool, dry weather.

| Perennial Crop Conditions – First Quarter – 2016 vs. 2015 | | |
|---|---|---|
| | **2016** | **2015** |
| Poor | 25% | 5% |
| Fair | 36% | 26% |
| Good | 34% | 62% |
| Excellent | 5% | 7% |

## Quarter Update

### Lending

AFSC authorized $155.2 million in new direct loans and guarantees for the first quarter of 2016-17, in comparison to the $172.6 million that was loaned in the first quarter of 2015-16. This lending facilitated an investment of $199.1 million in the province's agriculture, agri-industry and value-added sectors.

The total number of new farm loans for the first quarter of 2016-17 was 557, down from 575 in the first quarter of 2015-16. Under the Alberta Farm Loans Program, the 447 loans authorized also decreased from the 504 loans that were issued in the first quarter of 2015-16. To assist producers with their payments, some loan restructuring has occurred. Currently, arrears for the Alberta Farm Loan Program are at 0.5 per cent, consistent with the same period in 2015-16.

The Revolving Loan Program increased from 71 loans in the first quarter of 2015-16 to 110 in the first quarter 2016-17. In June 2015, an amendment was made to the Revolving Loan Program so that principal payments are based on the client's cash flow. This change has contributed to the increased participation.

For the first quarter of 2016-17, commercial loans were down to 21 from the 30 loans signed during the first quarter of 2015-16; however, the overall dollar value per loan increased. The arrears for commercial loans are nine per cent (six per cent at the same period in 2015-16). Alberta's slowed economy has contributed to the reduction of commercial loans and increase in arrears.

Through the Specific Loan Guarantee Program, AFSC processed six feeder association applications - either initial applications or renewals in the first quarter for a total of $1.65 million. One additional new application was also processed for a breeder association in the amount of $750,000. There are currently 23 separate outstanding guarantees loans for a total of $9.4 million.

The Value Added and AgriBusiness Program (VAAP) remained steady. For the first quarter of 2016-17, AFSC authorized 18 VAAP loans compared to 19 loans issued in the first quarter of 2015-16.

Alberta Flood Recovery Program interest rate rebates ended June 30, 2016. For this quarter, $82,667 was paid out. This brought the total amount paid out through this program to $1,407,433.

The total outstanding loan portfolio of $2.2 billion marked a 3.05 per cent increase at the end of the first quarter, which is up from the 2.1 rise at the end of last year's first quarter. This increase can be attributed to the increased dollar value of the loans.

## Lending Operating Results

| | Lending volume for year | | Portfolio loans outstanding | |
|---|---|---|---|---|
| | Number of loans | Amount lent ($M) | Number of loans | Amount outstanding ($M) |
| **2016-17 (1st quarter)** | | | | |
| Farm | 557 | 127.51 | 11,023 | 1,816.11 |
| Commercial | 28 | 22.92 | 840 | 274.43 |
| Value-Added and AgriBusiness | 18 | 4.72 | 387 | 153.32 |
| **Total** | **603** | **155.15** | **12,250** | **2,243.86** |
| **2015-16 (Annual)** | | | | |
| Farm | 1,858 | 445.26 | 10,905 | 1,755.47 |
| Commercial | 143 | 79.68 | 856 | 276.52 |
| Value-Added and AgriBusiness | 77 | 37.11 | 391 | 145.55 |
| **Total** | **2,078** | **562.05** | **12,152** | **2,177.54** |
| **2014-15 (Annual)** | | | | |
| Farm | 1,777 | 400.05 | 10,670 | 1,634.98 |
| Commercial | 172 | 77.68 | 926 | 276.63 |
| Value-Added and AgriBusiness | 84 | 45.14 | 410 | 165.88 |
| **Total** | **2,033** | **522.87** | **12.006** | **2,077.49** |
| **2013-14 (Annual)** | | | | |
| Farm | 1,770 | 391.59 | 10,386 | 1,487.61 |
| Commercial | 232 | 95.54 | 1,008 | 302.31 |
| Value-Added and AgriBusiness | 102 | 63.94 | 405 | 169.41 |
| **Total** | **2,104** | **551.07** | **11,799** | **1,959.33** |

M=Million

## Lending Administration Results

| | 2016-17 Target | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|---|
| Admin. cost ($M) | 26.47 | 6.77 | 26.47 | 24.51 | 22.97 |
| Write-offs ($M) | ** | ** | 2.5 | 3.5 | 1.75 |
| Operating surplus [deficit] | 0 | -1.6 | -2.4 | 4.51 | 12.53 |

M=Million
**To be determined as information becomes available.

### Lending Delivery Effectiveness

| | 2016-17 Target | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|---|
| Portfolio growth (% year over year) | 8.64 | 3.05 | 4.82 | 6.1 | 9 |
| Operating costs (% of portfolio) | 1.17 | .31 | 1.24 | 1.21 | 1.17 |
| Write-offs (% of portfolio) | ** | ** | .12 | 0.17 | 0.09 |

**To be determined as information becomes available.

## Insurance

As of June 30, 2016, AFSC had processed insurance coverage for 14.5 million annual crop acres. When processing is complete, it is expected that the total number of insured annual crop acres will be similar or slightly higher than last year's 14.7 million acres. The 2016 insured perennial crop acres increased to 7.8 million acres from 6.7 million acres the previous year.

During the first quarter, On Farm Inspections (OFI) completed 363 reseed claims. Early hail generated 1,277 hail claims, mostly in the Southern area of the province. There were 174 pre-harvest inspections completed for clients who elected to put their crops to another use, which compares to 449 reseed claims, 981 hail claims, and 265 pre-harvest inspections in the first quarter of 2015-16. Reporting on actual turnaround times for inspections will begin in the second quarter.

### Two new insurance products introduced for the 2016 crop year

**New Recognition for Organic Production Insurance**

Organic Alberta has assisted AFSC in finding a way to give organic producers the recognition they deserve. In 2016, the program will work similar to AFSC's standard production insurance programs. The exception is that certified organic producers will no longer be assessed for uninsured causes of loss, provided the producer follows the guidelines established by the Organic Standard and the Insuring Agreement.

**Malt Barley**

Developed with the assistance of the Alberta Barley Commission, a new end use option for malt barley insurance will provide more coverage for growers with malt contracts through a premium price compared to commercial barley

## AgriInsurance Operating Results

| | 2016-17 Target | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|---|
| Number of policies | 29,000 | 29,652 | 29,297 | 29,028 | 31,028 |
| Number of acres insured (M) | 36.12 | 36.01 | 35.58 | 34.96 | 36 |
| Amount of risk ($M) | 7,931.41 | 8,456.92 | 7,815.46 | 6,799.33 | 8,611.45 |
| Amount of premium ($M) | 615.23 | 706.13 | 617.99 | 584.83 | 780.43 |
| Amount of admin cost ($M) | 37.99 | 9.17 | 37.99 | 38.40 | 34.41 |
| Indemnities ($M) | N/A | ** | 474.25 | 373.22 | 308.56 |
| Loss to premium ratio (%) | N/A | ** | 76.7 | 63.8 | 39.5 |
| **Operating surplus ($M)** | **N/A** | ** | **143.27** | **229.03** | **469.09** |

M=Million
Note: Insurance performance measures include information for base programs as well as endorsements.
** Operating results will be available starting in the second quarter.

## AgriInsurance Delivery Efficiency

| | 2016-17 Target | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|---|
| Admin./policy ($) | 1,310 | 309 | 1,297 | 1,324 | 1,109 |
| Admin./acre ($) | 1.05 | .25 | 1.07 | 1.10 | 0.96 |
| Admin./risk (%) | .48 | .11 | .49 | 0.57 | 0.40 |
| Admin./premium (%) | 6.17 | 1.3 | 6.15 | 6.57 | 4.41 |

### Straight Hail Operating Results

During the first quarter, AFSC billed 3,111 straight hail subscriptions, covered $463 million of risk on 3.16 million acres and generated $39 million in premium. These numbers are consistent with last year. As of June 30, 2016, there were approximately 3,137 hail claims, which is slightly less than last year.

| | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|
| Number of policies | 3,111 | 3,757 | 4,617 | 4,895 |
| Number of acres insured (M) | 3.16 | 3.80 | 4.84 | 4.94 |
| Amount of policy risk ($M) | 462.81 | 546.39 | 711.40 | 589.83 |
| Amount of premium ($M) | 38.75 | 45.12 | 56.04 | 47.00 |
| Admin. cost ($M) | .62 | 1.79 | 2.31 | 2.22 |
| Indemnities ($M) | .83 | 32.60 | 61.24 | 37.76 |
| Loss to premium ratio (%) | ** | 72.3 | 109 | 80 |
| **Operating surplus [deficit] ($M)** | ** | **8.34** | **[8.84]** | **4.49** |

M=Million
** Operating results will be available starting in the second quarter.

## Western Livestock Price Insurance Program (WLPIP)

This quarter represents the start of the third year of the four-year WLPIP pilot program in which British Columbia, Alberta, Saskatchewan and Manitoba all participate. This quarter also represents the first time that the Advanced Payment Program (APP) was made available to livestock producers through WLPIP.

May 31 brought the 2016 WLPIP calf sales period to a close with a flurry of last day sales, which has become common. In Alberta the program insured approximately 147,000 calves this calf season, down from the 200,000 calves in 2015. Top coverage in May 2016 amounted to $202, a drop of $82 in comparison to last year's high of $284 in May.

Policies sold for all products in the first quarter of 2016-17 totaled 1,345, compared to 1,444 sold in the first quarter of 2015-16 (a decrease of 99 policies). Total insured units purchased this quarter totaled 1,029,077, which is 206,481 policies less than the 1,235,558 in 2015-16. Liability coverage dropped as well, in part due to cattle prices, which are softer in comparison to compared to last year. Liability coverage for this quarter was $184.6M, compared to $306M in the first quarter of 2015-16. Collected premium is up from $3.3M in the first quarter of 2015-16 to $4.7M this quarter.

| Province | Alberta | British Columbia | Saskatchewan | Manitoba |
|---|---|---|---|---|
| Policies | 1,345 | 136 | 998 | 319 |
| Liabilities | $184,643,746 | $13,545,968 | $108,682,088 | $25,741,204 |
| Premiums | $4,653,179 | $296,009 | $2,319,543 | $568,880 |

On June 7, the WLPIP Fed-Basis product became no longer available to cattle producers. The full WLPIP product recently underwent an independent review that determined the Fed-Basis program was not meeting intended targets set by both the livestock industry and AFSC, the program administrator. Currently-held Fed-Basis policies will be honoured, and the Fed-Basis Settlement Index will continue to be published until these policies are settled or expired. It is important to understand that the WLPIP Fed-Price product remains available to producers.

### WLPIP Operating Results

| | Policy option | Policies | Premiums ($ ,000) | Liabilities ($ ,000) | Indemnity ($ ,000) | Loss to premium |
|---|---|---|---|---|---|---|
| | Calf | 1,178 | 150,306,932 | 3,778,384 | 0 | 0 |
| | Fed | 41 | 15,389,022 | 309,281 | 0 | 0 |
| | Feeder | 125 | 18,775,792 | 559,894 | 0 | 0 |
| | Hog | 1 | 172,000 | 5,620 | 0 | 0 |
| **Total** | | **1,345** | **$184,643,746** | **$4,653,179** | **0** | **0** |

**To be determined as information becomes available.
N/A = Information not applicable

## AgriInvest

As of June 30, 2016, 26,000 Alberta producers had $570 million on deposit in their AgriInvest accounts for an average value of $21,922. This compares to 27,227 Alberta producers who had $535 million on deposit and an average value of $19,658 by the end of the first quarter in 2015.

### AgriInvest Balance of Funds on Deposit as of September 30

| Year | Number of Producers Depositing | Total Value of Contributions by Producer ($) M | Total Value of Contributions by Government ($) M |
|---|---|---|---|
| 2015 | 7,032 | 13,795 | 13,795 |
| 2014 | 22,118 | 61,251 | 61,251 |
| 2013 | 22,029 | 62,111 | 62,111 |

M=Million

## AgriStability

AgriStability claims are processed on a one-year lag basis. In the first quarter, AFSC ended the processing cycle for 2014 program year and started the 2015 program year. In the 2014 production year, grain prices were down from the highs at the end of 2012 and the start of 2013. As the year progressed, 2015 showed more stability in grain prices.

Forage crops were stable in 2014, but hay prices were extremely high in the summer and fall of 2015 due dry conditions throughout the province.

For 2014, cattle prices for calves, feeders, fed cattle, and breeding stock all saw large increases in prices over the year before closing at market highs. The 2015 year saw cattle prices climb until the middle-to-end of the summer, after which they started to drop.

Hog prices for the 2014 program year climbed to the highest prices in the last four years. Conversely, 2015 prices declined over the year, with finishers and market hog prices ending down on the year.

As of June 30, 2016, the 2014 program year has paid benefits to 6.4 per cent of the 13,769 claims received for a total of $28.92 million in payments. For the 2015 program year 3760 claims have been received to date while $6.32 million is issued in payments.

The average support level for producers has increased from $195,775 in 2013 to $222,657 in 2014. This is the result of high cattle and grain prices and a slight decrease of input costs.

### AFSC AgriStability Cost Effectiveness

| | 2016-17 (1st qtr.) | 2015-16 (Annual) | 2014-15 (Annual) | 2013-14 (Annual) |
|---|---|---|---|---|
| Admin. cost ($M)* | 3.85 | 15.93 | 18.41 | 18.01 |
| Less AgriInvest ($M) [deficit] | [-.35] | [-1.18] | [1.52] | [1.55] |
| Net AgriStability admin cost ($M) | 3.5 | 14.75 | 16.89 | 16.46 |
| Number of files processed | 2,756 | 14,864 | 15,244 | 17,825 |
| Cost per file ($) | 1,271 | 993 | 1,108 | 923 |

M=Million

* Income Stabilization administrative costs include Alberta's share of AgriInvest administration costs, which Benchmarks do not.

## AgriStability Claims by Industry

| Industry | Agristability claims ($M) | Denied AgriStability claims ($M) | AgriStability claims > $0 ($M) | AgriStability ($M) |
|---|---|---|---|---|
| **2015 Program Year** | | | | |
| Livestock | 338 | 8 | 16 | 0.20 |
| Crop | 618 | 3 | 55 | 3.11 |
| Other | 53 | 2 | 3 | 0.03 |
| **Total** | **1009** | **13** | **74** | **3.34** |
| **2014 Program Year** | | | | |
| Livestock | 3,963 | 57 | 617 | 32.81 |
| Crop | 7,385 | 100 | 932 | 16.83 |
| Other | 855 | 41 | 78 | 2.04 |
| **Total** | **12,203** | **198** | **1,627** | **51.68** |
| **2013 Program Year** | | | | |
| Livestock | 4,994 | 138 | 728 | 32 |
| Crop | 8,670 | 203 | 561 | 13.83 |
| Other | 1,295 | 59 | 135 | 1.63 |
| **Total** | **14,959** | **400** | **1,424** | **47.47** |
| **2011 Program Year** | | | | |
| Livestock | 6,586 | 179 | 825 | 23.94 |
| Crop | 9,790 | 352 | 1,188 | 19.47 |
| Other | 1,570 | 82 | 198 | 5.52 |
| **Total** | **17,946** | **613** | **2,211** | **48.93** |

M=Million